RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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Sept. 23 DJIA 2090.68; PTI 2758; A-D Ratio -10.76
Sept. 30 DJIA 2112.91; PTI 2763; A-D Ratio -10.47
Current Dow Yield: 3.66 ; Dow P/E: 12.5
Dow 200-day MA: 2035; DowPow: 835
Percentage of undervalued blue-chip stocks: 21%

THE MARKET: On a casual reading the best description of the current stock market can be summed up in a single word -- b-o-r-r-r-ing. But from a technical standpoint, the picture has become quite fascinating.

Ever since last March the market breadth (i.e., the advance-decline ratio) has been unwilling to confirm advances in the Dow. Each of this year's price/breadth non-confirmations has been followed by a sell-off in the market.

TECHNICAL TRAP: At this point, the market has placed itself in a literally untenable technical position. The problem is this: Any strong Dow advance from here is almost sure to produce another non-confirmation on the part of the A-D ratio.

Turn to the page 2 chart. Note that the Dow hit a high of 2087.37 on March 18. At the same time the advance-decline ratio recorded a high of minus 7.72. A decline followed. A few weeks later (on April 12) the Dow rose to a new high of 2110.08. But here the A-D ratio recorded a lower peak at minus 7.90. This second non-confirmation was followed by a decline which took the Dow down to 1941.48 on April 23.

Another rally got underway, and on July 5 the Dow advanced to a new post-crash recovery high of 2158.61. Again the A-D ratio refused to confirm; this time the A-D recorded a still lower peak at minus 8.48. This latest non-confirmation was followed by a decline which took the Dow down to 1989.33 on August 23. From there the Dow rallied again, but breadth on the most recent rally has been very poor, actually the worst seen on any rally this year.

So the picture ever since March 17 has been one in which the majority of NYSE stocks have refused to follow the Dow to new recovery highs. This, by the way, is typical bear market action. It tells us that under the guise of successive rallies in the D-J Industrial Average, the majority of Big Board stocks have been fading. It's a picture of continuing technical weakness, and I find myself wondering how much longer this kind of action can continue without triggering the next major down-leg in the bear market.

In a primary bear market I constantly look ahead and try to see what action by the Averages or by the A-D ratio might set the market up for trouble. However, if this were a primary bull market I would not operate in this manner. If this were a bull market I would tell my subscribers, "Sit tight, be patient; in due time everything will check out bullishly and confirm on the upside."

But in a bear market (as this one is), I watch for the Averages or the A-D ratio to get out-of-gear, thereby setting the stage for trouble ahead. The bear thrives on dis-harmony, and on Wall Street dis-harmony is signaled by non-confirmations and divergences in the Averages or in the A-D ratio.

Not only is there weakness in the majority of NYSE issues, but there is weakness within the D-J Industrial Average itself as seen in the relationship of the Dow to its own advance-decline line. The Dow A-D line tracks the daily differentials between the advances and declines of the 30 Dow stocks. Since July the Dow A-D has acted much weaker than the Dow. This tells us that even within the Dow itself a minority of the 30 Dow Industrial stocks have been doing the work during rallies -- hardly a healthy sign.

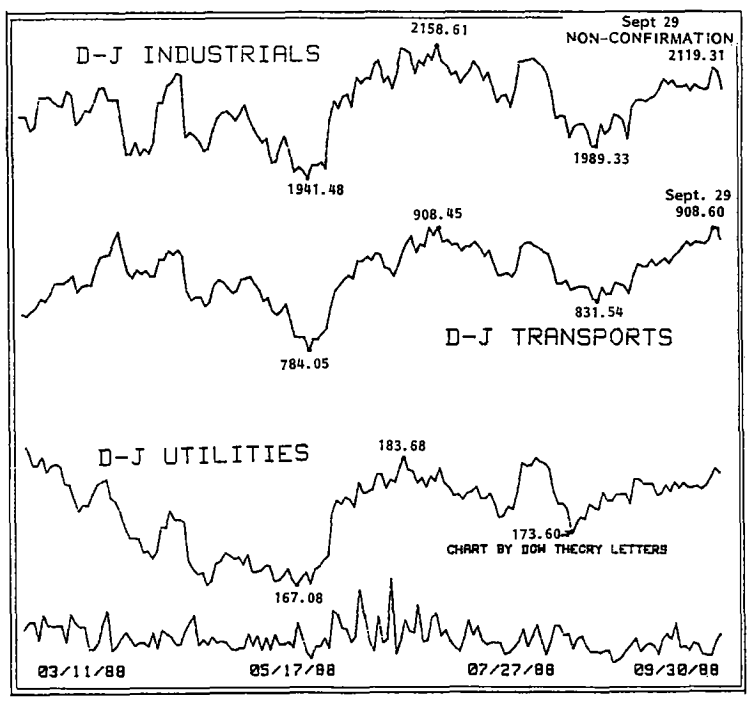
So the market may be boring, but the technical picture is quite interesting. And as I see it, the market is setting itself up for trouble -- specifically trouble in the form of upside non-confirmations by the A-D ratio any time the Dow rallies to new recovery highs.

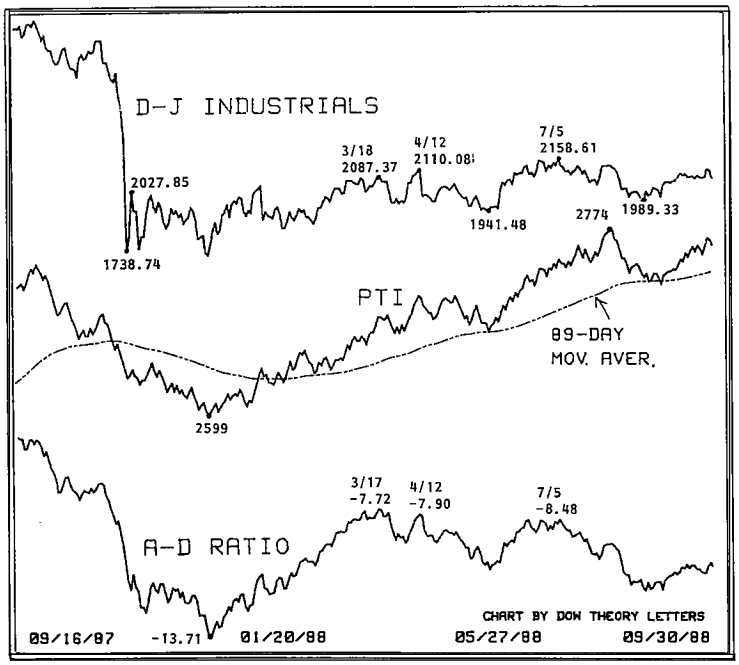
In reading dozens of advisory survices I'm surprised to see how many of them are singing the following popular song: "Everybody is bearish on the market; there are entirely too many pessimists around -- therefore the situation must be bullish." The absurdity of this situation is seen in the fact that so many advisory services are now optimistic or bullish -- based on their perception that "everyone else is bearish."

My own perception is that this 11-month trading range market which has followed the crash is driving most of Wall Street, the advisors, and the investment services up the proverbial wall. These "experts" are going a bit batty, and in their urge to "be bullish," they are dreaming up all sorts of nonsense such as the "everybody else is bearish" thesis described above.

A number of people have asked me why I continue to think that this will be a long, difficult, and painful bear market.I believe it will be a long bear market because this bear market is correcting a very speculative 13-year bull market (1974 to 1987), and bear markets often last one-third (or more) as long as the preceding bull market. Furthermore, we have not, since World War II, had a bear market that really corrected the excesses (and I'm talking about debt) in the economy.

I think this is fated to be a long bull market because our government today is more committed than ever before to "maintaining

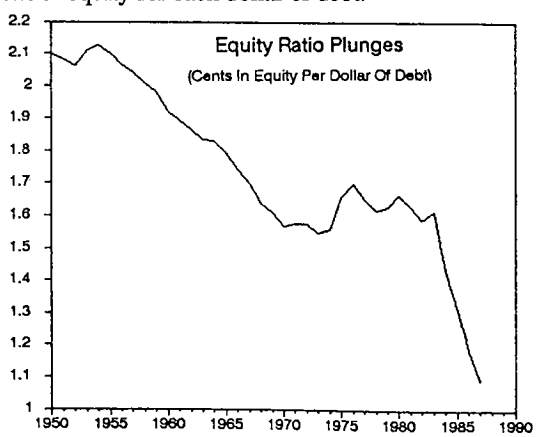




prosperity" here in the US. Of course, in reallity the government is incapable of maintaining prosperity just as the government is incapable of turning a bear trend into a bull trend. Washington's manipulations (via make-work projects and deficit spending) may temporarily hold back the bear forces, but in the end such manipulations will merely extend the bear market rather than ending it. Personally, I have always been of the opinion that any prosperity in America has occurred despite our government, not because of it.

Finally, I'm particularly worried about this bear market because I believe it's going to involve debt problems -- yes, even bigger debt problems than the Frankenstein monster of debt that we are wrestling with today.

Why do I worry about debt? Because over the last half dozen years corporate America has gone on a debt-building binge the likes of which the world has never seen before. One measure of this is the debt-to-equity ratio. The usual way to present this ratio is to show the amount of debt for each dollar of equity a corporation carries. But the *Holt Advisory* (290 Post Rd. W., Westport, CT 06880) has reversed the ratio. They show this long-term chart in terms of the amount of equity for each dollar of debt.



This chart by *Holt* is drawn from Federal Reserve statistics for non-financial corporations. Here we see the ratio very high during the 1950s with two dollars of equity for every dollar of debt. The ratio declined into the '70s, then rose during the early '80s. But look what has happened over the last six years. The ratio now shows a dollar of debt for every dollar of equity, a dangerous situation never seen in post-WW II America.

What will happen in the next recession when sales drop off, earnings turn down, and debt has to be serviced? The answer is bankruptcies and reorganizations, slews of them. And I don't have to tell you what's in store for the huge, multi-billion dollar junk bond market and to the over-leveraged corporations and to the shaky "leveraged buy-out" companies as this bear market gathers strength.

Eleven months have elapsed since the crash, and the October 19 low of Dow 1738.74 still stands inviolate. This has given hope and courage to many analysts, and they advance the following argument. From its August 25 high of 2722.42 to its October 19 low of 1738.74 the Dow lost 36.1% of its value. This is a major drop, exceeded in recent history only by the losses of 1973-74 (when the Dow lost 45%). But on the basis of the 36.1% drop in '87 the bulls are saying that "enough is enough, the bear market must be over."

To my mind, the argument is a thin one. For instance, from September 1929 to its November 1929 low, the Dow lost 48% of its value. That historic drop did not signal the end of the bear market. By the same token, I hardly think the 36% drop during August-October ended the current bear market.

There's no question in my mind but that the 11-month sideways action since the crash is allowing people to hope. But hope and a stiff upper lip never ended a bear market. Bear markets end in despair, give-up selling, and undervaluation in stocks. At present stocks are overvalued, yields are thin, and business is still good. So I'm sorry to say it, but this bear market is still in its first phase. There's more to come -- but it will take time.

In the last Letter I included a Warren Buffet quote in which he says that the beauty of the stock market is that it's like being in a baseball game in which you're a batter but there are no called strikes. You don't have to keep swinging; you can wait for the ideal ball. The ideal ball in this market will come when stocks are selling at "great values" again -- which means the average yields on the Dow back in the neighborhood of 6% or better.

Since 1949 I count eight periods when stocks were great values based on a Dow yield of around 6%. These were 1949-50, 1952, 1957, 1960, 1962 (marginal), 1966 (marginal), 1974, 1978-82. So sit tight, be patient -- there will be another great buying area somewhere ahead.

Note: Currently, I count only nine of the 30 Dow stocks in a bullish mode, in that (1) they are holding above their long-term moving averages and (2) they are showing positive relative strength. The bullish stocks are Aluminum Co., Beth. Steel, Boeing, Coca Cola, Int. Paper, Merck, Minnesota Mining, Philip Morris, Woolworth. McDonalds is on the verge of turning bullish, while IBM has turned bearish as have Chevron and Texaco with Exxon (with deteriorating RS) barely hanging on to a semi-bullish label. Navistar is increasingly bearish as is USX.

INVESTMENT POSITION: Ever since the bear market began last August I have tried to show the wisdom of investing in harmony with the primary trend of the market. In a bear market that means being out of stocks and basically in cash (plus high-grade bonds as described in the last Letter).

In the 14 months since the bear market began many investors have tried to beat the bear. But success stories are few and far between. In his latest report, *Merrill Lynch's* Chief Market Analyst, Bob Farrell writes, "So far this year, investors have not found it profitable to chase relative strength. Each group or sector that outperformed for two of three months subsequently became a laggard or vice versa."

That's true enough, and the process Farrell describes can be summed up in one word -- DISTRIBUTION. In a bear market

large, informed investors are constantly distributing stocks, and all periods of good news and all rallies are used as opportunities to move stocks from strong hands to weak.

Readers of *Dow Theory Letters* (if they followed my advice) completed their stock-distribution operations near the highs during April through August of last year -- well before the bear market started. In a primary bear market, stockholders find that the waiting game is a losing game. Time is against the stockholder when the primary trend is down.

VALUATION: The great values in stocks are found at or near bear market bottoms. The great distribution areas (selling areas) for stocks are seen at or near major bull market tops. The question: how do you identify such areas? One of the most helpful pieces of information is provided in the bi-weekly calculations by *Investment Quality Trends* located here in La Jolla.

IQ Trends monitors 350 blue-chip dividend-paying stocks and grades each stock on the basis of its dividend yield. *IQ Trends* notes that each stock has a dividend yield history. For example, from its history we know that Sears Roebuck is undervalued when it yields around 7% (which it did during 1980-82), and we know Sears is overvalued when it yields less than 3.5% (which it did in 1983 and 1987). Every two weeks *IQ Trends* tabulates the number of undervalued stocks in their 350-stock universe, and they have been doing that since 1966. The accompanying chart shows the results.

At major bottoms the percentage of undervalued blue-chips climbs above 73% and more often to around 82%, as witness the bottoms of 1970, 1974, 1978, 1980, and 1982. At major tops the percentage of undervalued blue-chips drops down into the 12% to 17% range, as witness the tops of 1966, 1968, 1972, and, most recently, 1987.

In other words, the percentage of undervalued blue-chips is a vital aid in identifying where we are as far as areas of great values (bottoms for buying) or areas of overvaluation (tops for selling). Courtesy of *IQ Trends* I am now running their percentage of undervalued blue-chips in each Letter, and doubtless you have noticed this statistic on the top right of page 1 along with the other market statistics.

Note that at present the undervalued percentage stands at 21%, meaning that only one out of five blue-chip stocks is currently undervalued. This is still in the area of market tops. At the next major bear market bottom I would expect to see at least 75% and probably more of the 350 blue-chip stocks in the undervalued zone. In brief, this study tells us that we are currently FAR from a bear market bottom.

Question: Russell, since we are so far from a bear market bottom and accompanying great buying area, what would you do with your money at this time?

Answer: I can tell you what I have done with my own money. I have about 80% of it in AA-rated municipal bonds (almost all issued in California, since I live here) and the rest in money market accounts with perhaps 4% of my assets in gold coins.

With the tax-free income from the bonds I either buy more bonds or hold it in a muni cash fund. This position suits me well. I like the way the bonds are acting, and I certainly like the income. Stocks in a long-term bear market paying an average of around 3.5% taxable don't interest me at all.

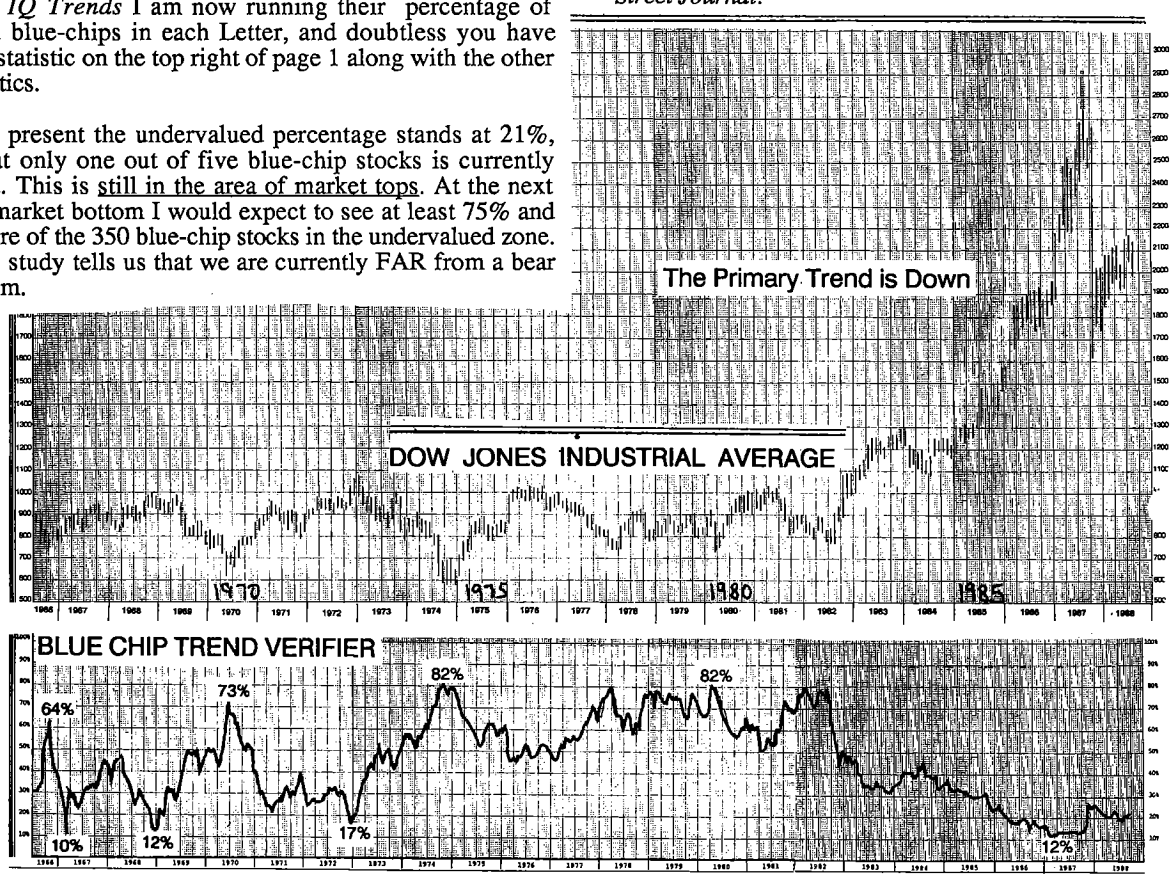
When we ultimately move into a major bear market bottom area (with stocks selling at around 6% yield and the undervalued blue-chip percentage near 80%), I'll probably make a major switch from bonds to stocks, plowing all additional income into stocks.

Questions and Answers: Question: If this is fated to be a long, tedious bear market as you suggest it will, what's going to happen to the securities business?

Answer: It's going to have a very rough time. Now obviously, I don't know how bad this bear market is fated to be or how long it's going to run. I simply use my intuition and my experience in coming up with my "guess/answer."

But it can get pretty grim on Wall Street. When I graduated from college back in 1946 (of course that was just after WW II) people didn't even think about Wall Street. Volume on the NYSE was running a million shares or so a day, and only one fellow from my high school class of 98 boys ended up working for a securities firm. Interest in stocks was almost non-existent, so I've seen it slow to very slow to dead, believe me I have.

I doubt if in our lifetimes we'll ever see that kind of disinterest in the stock market, but given a long bear market interest can really die out. Some of the problems of this massive post-crash "slowdown" on Wall Street were documented in a Sept. 25 piece in the *Wall Street Journal.*



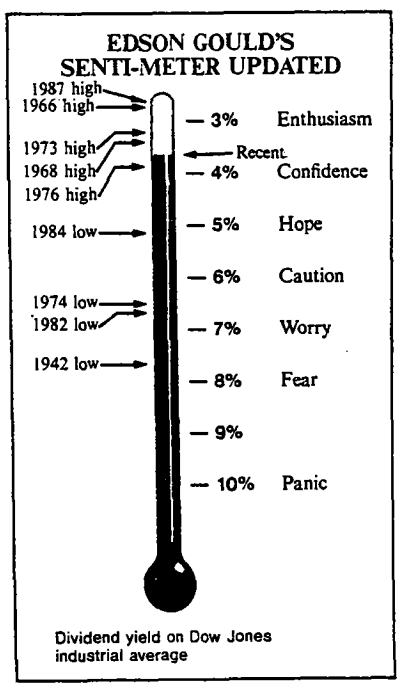
Question: Russell, as per your instructions, I'm out of the market, I'm content, my funds are safe, and I no longer rush to the financial section of our local paper each evening to scan the stock quotes. But tell me, while the bear market is on, why should I continue to read your Letters? Why shouldn't I just take a vacation from the stock market until the bear market is over?

Answer: What I'm writing about and what we're dealing with entails a lot more than just the NYSE. I was talking to Ron Insana, one of the "anchors" for Financial News Network a few weeks ago, and I asked him how he liked his work. He said, "Richard, this is the most fascinating thing I've ever done in my life." I feel the same way. The markets have to do with everything that is happening, both in the US and throughout the world.

I try to get that excitement across in the Letters. One of the reasons I've managed to stay in business for 30 years (I still can't get used to that number) is that I've been able to zero in and write about the exciting, important, and profitable areas of the markets. In the 1960s it was strictly stocks, in the '70s it was stocks and then gold, silver and collectibles, in the 1980s it was stocks again and more recently bonds and income-producing instruments. In the 1990s it may be the financial equivalent of the song from the John Travolta movie, entitled "Staying Alive."

In the Letters I deal with what fascinates me and what I am struggling with myself. I'm not presenting group opinions or consensus thoughts. Frankly, I almost never read a committee report or a group paper that's worth a damn. The ideas that interest me alway come from thinking individuals. I try to be one of those individuals.

Question: Everybody, or at least a lot of the so-called experts, are saying that "the worst is probably over." Russell, how you can be so sure that these highly respected experts are wrong.



Answer: This is the question I most frequently get today. There aren't many sure things in the stock market, and I've seen the best brains on Wall Street be dead wrong. But if there is one thing that is certain, it is the broad swings to emotional extremes which seem periodically to envelop the nation and its markets.

Nobody has ever figured out why, but all history tells us that mankind and the markets are subject to these extended emotional swings. The swings run from deep depression and gloom to outlandish optimism and then back to black pessimism again. Just as night follows day, human nature has always run to extremes

The year 1987 was a classic example of enthusiasm, optimism, and pure greed. My old friend, the late Edson Gould (a great market analyst), invented what he termed his "Senti-Meter," based on the Dow yield. Edson used this device to quantify the level of emotion in the market. I have updated Edson's Senti-Meter below. Today, with the Dow at a 3.7% yield, the market emotion is below "enthusiasm" but higher than "confidence."

We are now on the long bear market path to "caution" and thence to "worry" or "fear." Why will it happen? I have no perfect explanation -- all I can do is describe the process. The bull market is dead. The bear market is here. Bear markets end in pessimism, fear and disillusionment. They always do, all of them -- and I don't think the bear market that began in 1987 is going to be the exception.

Question: Russell, I note that you run an ad in both *Barron's* and *Investor's Daily*, and that ad includes the picture of a bear. Why do you do this?

Answer: I run the only consistently bearish ad in any publication that I know of. I've run this bear ad ever since I called a bear market last October 15. I want people to know that I've taken a stand on the market, as opposed to all the pussyfooting and waffling that's going on. At any given time the primary trend of the market is either bullish or bearish. Consequently, my ads always contain a picture of a bull or a bear. I want people to know where I stand on the primary trend of the market.

Question: Do brokerage houses take Dow Theory Letters? If so, how come most of them are still fairly optimistic about the market?

Answer: Just about every major brokerage house subscribes to *Dow Theory Letters*. Many brokers take the *Letters* through their libraries and some take it via their senior executives. Wall Street suffers severely during bear markets. But the heads of Wall Street firms know that they're no different than anyone else -- they must deal with reality or go broke. I like to think that's why brokers subscribe to *Dow Theory Letters* -- even during bear markets.

Question: What do you see coming up for money rates?

Answer: The inflation/deflation equation is very confused now. If you look at gold and oil and the commodities, you'd have to say that deflation was entering the picture. The CRB Commodities Futures Index just broke below 240, and almost across the board commodities have topped out.

But on the consumer front prices continue to creep up. The CPI is running at an inflation rate of about 5%. All the consumer items such as autos, cigarettes, theatre tickets, restaurant prices, seem to be on an never-ending creep higher.

I think the Fed is confused on inflation, but they are keeping the tell-tale Fed Funds rate fairly high or above 8%. The bill rate climbed to above 7% and then leveled off. The long-term T-bonds are holding just above 9%. The muni bonds have been the stars, dropping steadily in yield from almost 8% last April to below 7.5% at present. Prognosis: Confusion reigns.

Question: It may be a bear market, but a number of stocks are going up. Why don't you recommend a few of them, or are you against making money?

Answer: I'm all for making money, but I want the odds on my side. In a bear market the odds for making money in stocks are against you. Before a bear market is over, roughly 85% of all stocks will be down (in a severe and extended bear market 95% of all stocks will be down). To pick the stocks that will buck the trend is very difficult. But if you can do it, more power to you. Personally, I'll keep my money dry and ready for the next bull market. I like the odds on my side (which means holding stocks only during bull markets).

Question: What's the meaning of this dull, listless market? Why is nothing happening?

Answer: Buying interest in this market is dying out (except for very selective and isolated areas where there is news of a takeover or a merger). Buying power is drying up because the public and the institutions are puzzled. People are either frightened or unable to figure out what's going on. At the same time there isn't any real selling pressure either, and this combination, dearth of buying and lack of selling, is giving us "the 1988, do-nothing market."

One current phenomenon is worth noting, however: Good news on a stock is greeted with apathy, while rotten news (such as poor earnings) sends a stock south in a hurry. That's typical bear market action. If this were a bull market, bad news wouldn't affect stocks at all. In fact, in a bull market bad news will often send a stock rallying, since investors (during bull markets) frequently use any bad news as a golden opportunity to accumulate stocks.

NOTES AND QUOTES: A few Letters back I reported that my daughter, Betsy, was beaten up and pistol-whipped by a thug in Hollywood. That was the bad news. Here's the good news: Betsy's tough, and she's in fine shape now. Further good news: Betsy's engaged to Vince Van Patten (son of Dick Van Patten of TV's "Eight is Enough"). Vince has been a top-ranked pro tennis player, and before that a child TV star. He's a great guy, and I think they're both lucky to have found each other.

* *

Are you getting tired of magazines listing "The Ten Most Powerful People in New York," "The Twenty Richest People in the US," "The Hundred Biggest Corporations in America"? All of this has one concept in common -- POWER. People (and certainly magazine editors) are fascinated with power and never so much as now. In fact, sometimes I think the desire for power runs the world. Examine all history, and you will see that 90% of it is based on some person or some group's insatiable drive for power.

Along these lines, I thought this quote by Mario Cuomo was worth repeating: "Private power is always wealth or leverage over wealth. If Donald Trump comes to me and says he can build a $270 million stadium without my money, that's power."

The latest trappings of power -- own a name hotel. Trump recently bought NY's Plaza Hotel for a mind-blowing $400 million, and he promises to make it the finest hotel in the world. Billionaire Robert Bass owns the Westin chain. Caroline Rose Hunt owns the plush Bel-Air in LA. The Sultan of Brunei owns the famous Dorchester Hotel in London. Merv Griffin owns the landmark Bevery Hills Hotel.

* *

In 1986 (the lastest year that Treasury statistics are available) 92,600 Americans earned annual incomes above $500,000. These wealthy people paid a total of $48 billion in income taxes. Now consider this: Today the US has a $1 trillion budget which means that our government spends $2,740,000,000 (yeah, that's billions) a day. That means that rich people's taxes cover exactly 17.5 days of federal spending. Would you say that this nation is going nuts or what?

* *

Instant electronic communications is changing the world. A few years ago I wrote that the Russian leaders banned computers for the populace (including the schools) since computers provide access to information, something the Russian leaders are mortally afraid of. But the alternative for Russia was to remain ignorant and basically primitive while the rest of the world passed her by.

The outcome of the dilemma was computers for Russia. The spectre of booming prosperity in S. Korea, Japan, Hong Kong, Singapore, and Taiwan was probably too much for the Russian leaders. So Gorbachev won, and glasnost and perestroika are the new buzz words.

Emerson wrote, "Nothing is as powerful as an idea whose time has come." The idea: access to information -- leading to freedom, TV for the masses, finding out what the other guy is doing, finding out that central planning and communist economics doesn't work, finding out that other people have a lot of what you don't have. With electronics and instant information nations now accomplish in five years what it used to take a generation to do. Look at the build-up of the Asian nations, look at the "overnight" industrialization of S. Korea and Taiwan.

It's obvious that Gorbachev understands all this, and it's obvious that he sees the danger in the current Russian position of spending huge amounts on the military while the Russian people stand in lines in front of stores with empty shelves. Furthermore, and this is new -- the Russian people are speaking up -- they are telling Gorbachev and the Russian leaders that they are fed up. The people want action, not words.

So Gorbachev is pressured on one side by the people. And on the other side Gorbachev is pressured by the reactionary KGB plus the conservatives in his party and by the vested interests who want to retain power. Gorbachev is dancing on the tightrope, but he is going for the computers and the modernization of Russia. Whether he can bring it off, whether he can survive, is one of the major questions in the world today.

In order to modernize and boost economic development, Gorbachev knows that he has to cut back on military expenses -- in a big way. This means pulling out of Afghanistan and moving toward a general policy of (1) convincing the US that he means business, (2) getting friendly with a suspicious China, (3) obtaining loans, hard currency, and industrial help from the West.

In the US the conservatives, the military and most in the military/industrial complex are highly skeptical of Gorbachev's intentions. Bush seems to be pretty much on the side of the skeptics, while the more liberal Dukakis wants to cut down on the US military. Which side is correct? Where does the future lie? Can we trust the Russians? I honestly don't know, but I am convinced that Gorbachev sees Russia as a backward nation that must industrialize fast or sink into the twilight of history.

So I'm watching to see whether Russia takes the bull by the horns and starts to de-militarize unilaterally or even if Russia continues to push for disarmament treaties. If she does, Russia will be putting intense pressure on the US (because of our towering military expenses) to cut back as well. If that happens, among other things, the US will face a lot of economic dislocation -- and a lot of dissent. For instance, in California one out of every five jobs is connected to defense.

I'm writing all this because I believe this is going to be one of the big stories of the coming decade. And we should be prepared for it.

* *

Item: Young people in China are hungry for the latest in Western wear. Fashion's hottest new magazine, *Elle*, is going to the People's Republic of China. About 100,000 issues of Elle's 122-page inaugural issue are being sold in more than 600 Chinese cities and provinces for roughly $1.80 a copy.

* *

The bloom is off the rose for the British economy. Early this year Britain's treasurer announced a huge $7 billion tax cut. Unemployment has been dropping steadily for the past two years. But now Britain's burgeoning consumer demands have been producing record trade deficits and the bank rate has boomed to 12%. The whopping rates have punctured the British housing boom and saddled Brits with huge mortgage rates of 12.75%.

* *

Futurism: The car of the future could be pollution-free and solar-powered. In mid-September in Visalia, Calif., the nation witnessesd its first solar car race. Henry Worden of MIT (he's called "the Henry Ford of solar cars") has designed and built six of 10 working USA solar autos. His current car, sponsored by Dow Chemical, won the160-mile race (100 cars were entered) in three hours, five minutes. Worden says, "I plan to produce a computer solar car that will sell for about $3,000."

* *

California's Attorney General Van de Kamp is asking for $9.4 million to fight the street gangs, which he calls a far bigger menace than the mafia.

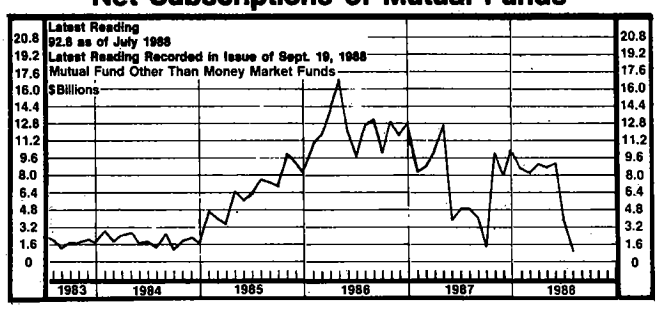
LA has 70,000 gang members, and the gangs are now spreading out to major cities, setting up drug networks and committing

violence. Last year in LA alone gangs accounted for 400 deaths. Said Van de Kamp, "These are grim reminders that groups like the Crips and the Bloods are no longer street gangs in the traditional sense. They are far-flung distribution networks for Columbian cocaine -- with elaborate organizations and murderous profit motives for eliminating competition."

* *

In the last Letter (page 1) I showed the parabolic rise in volume on the NYSE and I indicated that the termination of that curve spelled the end for high volume for probably many years to come. The decline in volume spells hard times for Wall Street, but no place is "fat city" forever. A second area of trouble for Wall Street is seen on this chart (courtesy of *Media General Financial Weekly*) showing what's happening to the sales of mutual funds. The chart speaks for itself.

Net Subscriptions of Mutual Funds



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Could this be true? They tell me that today in Texas if you buy a toaster ,they give you a bank for free.

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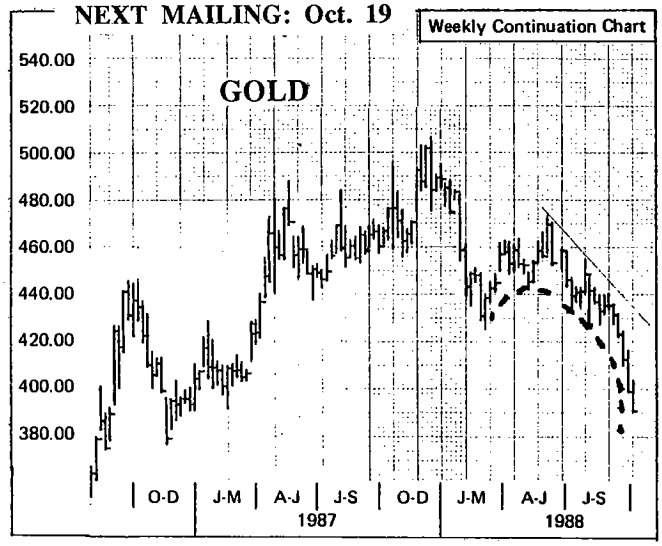
Many thanks to all those subscribers and old friends who sent congrats on my Letter number 1000. A few true optimists said that "they hope I write 1,000 more." Yeah, thanks a lot -- let's see, it took me 30 years to write 1,000 Letters, if I write 1,000 more I'll be 94 when I hit Letter 2,000. Mmmm, maybe I can do it, yes, yes, I'll do it! But I warn you, at age 100 I'm quitting this business, it's just getting too darn tough.

GOLD: The sentiment toward the precious metals is now overwhelmingly bearish. According to *Market Vane's* "Bullish Consensus," the bullish consensus for platinum is now 25%, the bullish consensus for silver is down to 12%, and the bullish consensus for gold is a low 25%. These figures indicate an extraordinary percentage of advisors who are pessimistic about the precious metals.

There's no question but the charts have all broken down on gold. There are only two things going for gold at the moment. The first is the almost universal, extreme pessimism as described above. The second is the steep collapse which reached an almost straight-down phase as shown on this weekly chart (chart coutesy of *Dunn and Hargitt*).

The action on the chart is tantamount to a parabolic curve in reverse. This type of formation (I have outlined the formation via the dotted line) often winds up the downside action. Actually, what the "parabolic curve in reverse" is -- is simply panic action, a picture of prices plunging with buyers "throwing it in." I have studied many such patterns in both stock averages and in individual stocks, and I have noted that a parabolic curve in reverse often terminates a downside move. We will see whether this holds true for gold. If it does, gold (London spot price) should tend to hold at or above the 390 level.

For the benefit of new subscribers, I have been advocating a program of dollar-averaging in bullion gold coins (Krugerrands, Coronas, Maple Leafs, American Eagles). This means buying a fixed-dollar amount of gold coins each month. To repeat so there are no mistakes, I want subscribers to accumulate gold coins, the metal itself, not gold shares, not gold certificates, not gold held by



your broker, but gold held by you in your bank vault. A lower gold price, as far as I am concerned, means more gold for your buck, and from a long-term accumulation standpoint, the lower the price, the more of the metal we can buy for our money.

LATE NOTES: No sooner did I pronounce the stock market "boring" (see page 1) than some excitement entered the picture. On September 29 the Dow surged 33 points while the Transportation Average closed at a new post-crash recovery high of 908.60 (this betters the July 5 Transport high of 908.45 -- see page 1 chart). **BUT** on the same day the Dow closed at 2119.31, well **BELOW** its July 5 high of 2158.61. Thus an important non-confirmation exists in that the Industrials failed to confirm the new high in the Transports.

On September 30, perhaps reacting to the non-confirmation, the market sold off with the Dow down 6.40 for the day. On October 3 the market sold off again with the Down around 24 points by mid-day. As I stated on page 1, the Dow itself has been weak internally, with the Dow advance-decline line failing by a wide margin to keep up with the Dow on rallies. Thus, the Dow non-confirmation of September 29 should have come as no surprise.

The September 29 Dow advance above 2100 represents the Dow's fourth attempt this year to mount a rally from above the 2100 level. Again I'll state Edson Gould's old rule:, "The market may try three times to move above a given level. On the fourth attempt it will usually succeed big -- or fail big." It will be interesting to see whether Gould's observation applies to today's market.

Next problem: Even if the Dow does close above 2158.61 (see page 2 chart), this will simply add another price/breadth non-confirmation to the series that began last March at minus 7.72 on the A-D ratio as described earlier in this Letter.

Please study that page 2 chart carefully. What we see here is not a minor series of non-confirmations between the Dow and the A-D ratio, these are major non-confirmations occurring over a period of many months.

In the past, a series of price/breadth non-confirmations covering a period of six months or more has led to major trouble in the stock market. Maybe "this time it will be different." At any rate, from a technical standpoint, this market is now anything but boring.

I find this whole period particularly interesting because the market's shakiness is occurring in the face of widespread predictions by the economic "experts" of "no trouble and no recession until 1990 or even 1991." I have noticed in the past that trouble has a habit of arriving when the experts are placing the next recession "a year or so away."

PS: I did an interview today for Ted Koppel's "Nightline" program which, I am told, is scheduled for the evening of October 19.